



DEPARTMENT OF  
**FINANCE**

ARNOLD SCHWARZENEGGER, GOVERNOR

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September 26, 2008

Mr. Mark Leary, Executive Director  
California Integrated Waste Management Board  
1001 I Street, MS-1  
P.O. Box 4025  
Sacramento, CA 95812-4025

Dear Mr. Leary:

**Final Audit Report—Lucas Oil Products, Inc., California Used Oil Recycling Fees**

Enclosed is the final report of Lucas Oil Products, Inc.'s (Lucas) Used Oil Recycling Fee Returns for the period July 1, 2006 through June 30, 2007. The Department of Finance, Office of State Audits and Evaluations (Finance), conducted the audit in accordance with an interagency agreement between Finance and the California Integrated Waste Management Board.

The audit determined whether Lucas accurately reported the used oil recycling fees and oil sales in compliance with state law. Based on the audit, Lucas underreported 104,374 gallons of lubricating oil which resulted in an underpayment of \$16,700 in used oil recycling fees.

We appreciate the assistance and cooperation of Lucas' staff during our audit. The enclosed report is for your information and use. We have also sent a copy to Lucas. In accordance with Finance's policy of increased transparency, the final report will be placed on the Finance website.

If you have any questions regarding this report, please contact Kimberly A. Tarvin, Manager, or Rich Hebert, Supervisor, at (916) 322-2985.

Sincerely,

David Botelho, Chief  
Office of State Audits and Evaluations

Enclosure

cc: On following page

cc: Mr. Tom Estes, Deputy Director, Administration and Finance Division, California Integrated Waste Management Board  
Ms. Julie Arico, Accounting Administrator, Administration and Finance Division, California Integrated Waste Management Board  
Ms. Susan Villa, Branch Manager, Administration and Finance Division, California Integrated Waste Management Board  
Mr. George Mendoza, Audit Manager, Administration and Finance Division, California Integrated Waste Management Board  
Mr. Robert Patison, Executive Vice President, Lucas Oil Products, Inc.  
Ms. Rhoda Binckes, Controller, Lucas Oil Products, Inc.

# AN OIL RECYCLING FEE AUDIT

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## Lucas Oil Products, Inc. Used Oil Recycling Fee Returns For the Period July 1, 2006 through June 30, 2007

Prepared By:  
Office of State Audits and Evaluations  
Department of Finance

## **MEMBERS OF THE AUDIT TEAM**

Kimberly A. Tarvin, CPA  
Manager

Richard Hebert, CPA  
Supervisor

### Staff

Alice Yip

This report is also available on our website at <http://www.dof.ca.gov>

You can contact our office at:

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## EXECUTIVE SUMMARY

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In accordance with an interagency agreement with the California Integrated Waste Management Board (Board) the Department of Finance, Office of State Audits and Evaluations, performed a compliance audit of the used oil recycling fees and industrial oil sales reported by Lucas Oil Products, Inc. (Lucas).

The objective of the audit was to determine whether Lucas accurately reported lubricating oil sold, transferred, or used in California, and remitted the proper fees owed in accordance with the California Oil Recycling Enhancement Act for the period July 1, 2006 through June 30, 2007. The audit was conducted in accordance with *Generally Accepted Government Auditing Standards* (GAGAS), issued by the Comptroller General of the United States.

Based on the audit, Lucas underreported 104,374 gallons of lubricating oil which resulted in an underpayment of \$16,700 in used oil recycling fees.

This report is intended for the information and use of Lucas and the Board and is not intended to be and should not be used by anyone other than the specified parties. However, this restriction is not intended to limit the distribution of this report, which is a matter of public record.

# BACKGROUND, SCOPE, AND METHODOLOGY

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## Background

The Legislature enacted the California Oil Recycling Enhancement Act (Act) (Public Resources Code, Sections 48600 through 48691) to reduce illegal disposal of used oil, and to recycle and reclaim used oil in order to recover valuable natural resources, and to avoid damage to the environment and threats to public health. This Act gives the California Integrated Waste Management Board (Board) the authority to adopt and implement a used oil recycling program, and to collect fees from oil manufacturers at a rate of 16 cents for each gallon of lubricating oil sold, transferred, or used in California. These fees support the California Used Oil Recycling Fund from which various state and local programs are operated. These programs help promote local efforts to recycle used oil before harmful environmental impacts can occur.

Lucas Oil Products, Inc. (Lucas) blends lubricating oils and other products for sale in California, the United States, and worldwide. Bulk oil is transferred from the Lucas facility in Indiana and blended in Corona, California for resale. Lucas' corporate headquarters is located in Corona, California.

## Scope

The Department of Finance, Office of State Audits and Evaluations, conducted a compliance audit of the California Used Oil Recycling Fee Returns submitted to the Board. The objective was to determine whether Lucas accurately reported the lubricating oil sold, transferred, or used in California, and remitted the proper fees in accordance with the Act for the period July 1, 2006 through June 30, 2007.

We conducted our audit in accordance with *Generally Accepted Government Auditing Standards*, issued by the Comptroller General of the United States. In order to design adequate procedures to evaluate the California Used Oil Recycling Fee Returns, we obtained an understanding of the related internal controls. Lucas is responsible for ensuring accurate reporting of the used oil recycling fees and oil sales and ensuring compliance with the Act.

## Methodology

To determine whether Lucas reported the used oil recycling fees and oil sales in accordance with the terms and conditions of the Act, we performed the following procedures:

- Interviewed key personnel.
- Obtained an understanding of the internal controls related to the preparation of the California Used Oil Recycling Fee Returns (Returns).
- Reviewed Lucas' accounting records.

- Traced the gallons of lubrication oil sold in California reported on the Returns to shipping invoices, bills of lading, purchase orders, delivery tickets, and other relevant documents.
- Determined whether valid exemption certificates were on file for exempt transactions claimed on the Returns.

The results of the audit are based upon our review of documentation and other information made available to us. The audit was conducted during May and June 2008.



The Department of Finance, Office of State Audits and Evaluations completed an audit of the Used Oil Recycling Fee Returns. Based on the audit procedures performed, the following findings requiring corrective action were identified.

**FINDING 1      Due to an Incorrect Calculation Method, Lubricating Oil Fees Were Underpaid by \$16,700**

Condition: Lucas underreported 104,374 gallons of lubricating oil sold subject to the used oil recycling fee resulting in an underpayment of \$16,700 as illustrated in the table below. The production manager used estimated production data instead of accounting records to prepare the Used Oil Recycling Fee Returns. Furthermore, Lucas did not obtain the required exemption certificates for some transactions claimed as exempt from the used oil recycling fee.

<b>Lucas Oil Products, Inc. Used Oil Recycling Fee Returns For the Period July 1, 2006 through June 30, 2007</b>			
<b>Categories</b>	<b>Sales and Fees Per Fee Payer Returns</b>	<b>Sales and Fees Per Lucas Sales Records</b>	<b>Differences</b>
Gross Lubrication Oil Sold (Gallons)	1,416,014	1,769,838	353,824
Less: Exempt Transactions (Gallons)	1,032,653	1,282,103	249,450
Total Lubrication Oil Sold (Gallons Subject to Fee)	383,361	487,735	104,374
Underpaid Fees (\$0.16 per gallon)	\$61,338	\$ 78,038	\$16,700

The California Code of Regulations, Title 14, Section 18626 states that all sales or transfers of lubricating oil in the state by an oil manufacturer are subject to oil recycling fees unless exempted. A seller is exempt from responsibility for the fee when the purchaser certifies in writing to the seller, in a timely manner, that the lubricating oil will be used in an exempt manner, as provided in Public Resources Code 4865.

- Recommendation: Lucas should perform the following:
- Use actual sales data to accurately report lubricating oil sales and calculate the recycling fees.
  - Obtain exemption certificates from California purchasers for lubricating oil that will be used in an exempt manner.
  - Provide training and adequate access to the accounting records to the individuals preparing and signing the Return.
  - The underreported fees of \$16,700 to the California Integrated Waste Management Board.

**FINDING 2                      Sales Contracts and Invoices do not Separately Identify the Amount of the Used Oil Recycling Fee**

Condition: Because Lucas elects to pay the recycling fee for its California customers, Lucas did not include a separate line on the invoice showing the 16 cent per gallon fee or include this information in the sales contracts.

In order to ensure that the fees for lubricating oil sold or transferred in California have been paid, Title 14, California Code of Regulations, Division 7, Chapter 8, Section 18625 requires that sellers of lubricating oil notify their customers whether the fees have been paid at the time of sale. Whether on the sales invoice, or in the sales contract, the seller must clearly state either that the fee is included in the amount paid by the buyer, or that the fee has been paid separately by the seller to the Board. Furthermore, Public Resources Code Section 48650.7 requires that for any transaction involving a total volume of oil subject to payment pursuant to Section 48650 in excess of 10 gallons, the invoice or other form of accounting of the transaction must identify the amount of the payment separately from the cost of the oil. This section applies even if the invoice amount of the fee is zero.

Recommendation: Lucas should notify its California customers that the fee is paid by Lucas and separately identify the fee amount per gallon on the invoice or contract, even when the fee charged directly to the buyer is zero. Additionally, Lucas should track the fees paid by it on behalf of its California customers in their accounting records.





## *The World Leader in Heavy Duty and High Performance Lubricants*

### *Corporate Headquarters*

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09/03/2008

Department of Finance  
Office of State Audits and Evaluations  
300 Capitol Mall, Suite 801  
Sacramento, CA 95814

To Whom It May Concern:

Lucas Oil Products, Inc is in receipt, by e-mail on September 3, 2008, the Draft Audit Report – Lucas Oil Products, Inc., California Used Oil Recycling Fees for the audit period July 1, 2006 through June 30, 2007. We acknowledge and accept the Draft Audit Report. Lucas Oil Products has implemented the recommendations outlined in the report.

Lucas Oil Products acknowledges the Draft Audit Report calculated underpayment of \$16,700.00. Lucas Oil Products, Inc will make payment of the reported underpayment. It is our understanding that we are to await payment of the \$16,700.00 until notified by the Integrated Waste Management Board.

Sincerely

Rhoda B. Binckes  
Controller